199925050

Internal Revenue Service

Department of the Treasury

Washington, DC 20224

Uniform Issue List: 401.00-00

Person to Contact:

Telephone Number:

Refer Reply to:
OP:E:EP:T:3

Date:
MAR 29 [illegible]

Attention:

Legend:

Company A =

Company B =

Controlled Group C =

Controlled Group D =

Company E =

Company F =

Division G =

Plan X =

Dear

This is in response to your request for a ruling, submitted by letter dated December 3, 1998, and supplemented by a letter dated January 14, 1999, regarding the taxation of proposed distributions from a plan described in section 401 (k) of the Internal Revenue Code (the "Code").

Company A, through its subsidiaries, is engaged primarily in private passenger automobile and specialty property and casualty insurance businesses, and in the sale of tax-deferred annuities and certain life and health insurance products. Company A is a member of Controlled Group C. Company A sponsors Plan X, a multiple employer retirement.

Plan X has been adopted by other members of Controlled Group C for the benefit of its eligible employees. Company B is an employer related to Controlled Group C, but Company B is not a member of Controlled Group C. Company B is a member of its own controlled group of corporations ("Controlled Group D"). Company B, its subsidiaries, and other

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members of the Controlled Group D have adopted Plan X. Plan X provides for a Section 401(k) Contributions Account, Matching Contributions Account and a Retirement Contributions Account.

On September 14, 1998, Company B and certain of its subsidiaries entered into an asset purchase agreement (the "Agreement") to sell one of its divisions (Division G) to Company E an insurance subsidiary of Company F, an unrelated purchaser. The sale was completed on December 1, 1998. Under the Agreement, over 85 percent of the assets of Division G were acquired by Company E.

Prior to the sale of Division G, Company B managed and operated its property and casualty insurance business as four major business segments. These divisions were: (1) nonstandard automobile insurance group; (2) specialty lines insurance operations; (3) personal lines segment; and (4) commercial lines division (Division G). Prior to the sale, Division G had its own management (including executive management), clerical, underwriting, claims processing, marketing and sales staff. The management staff was responsible for making its own personnel decisions (i.e., hiring and firing) regarding the employees of Division G. Division G had its own distinct and separate clients which were sold to Company E. Each division had its own sales, service and support staff. All employees only performed services for the specific division for which they were hired. The sales, service and support staff were not shared among any of the different divisions.

Each of the four divisions of the property and casualty insurance operations were subject to central financial, accounting, investment systems, information systems, payroll, human resources, and legal services. However, the financial aspects of Division G were managed independently and the division had its own budget. Each of the four divisions in the property and casualty insurance group had its budget adjusted to account for its portion of the costs of these shared services. Indirect costs such as rent and utilities were allocated to each division. Separate financial statements were maintained for Division G. The assets and liabilities of the Division G were specifically identifiable. Division G had profit centers and accounts receivable and payable, which were separate from the other three divisions.

Company E has not adopted Plan X and is not a participating employer whose employees accrue benefits under Plan X. Furthermore, neither Plan X, nor any part of it has been merged or consolidated with any employee benefit plan maintained by Company E. No assets or liabilities of Plan X have been transferred to a plan maintained by Company E. All of the employees of the Division G that was sold to Company E who were covered by Plan X became employees of Company E.

Based on the foregoing, you request the following rulings:

1. The disposition of Division G by Company B pursuant to the Agreement constituted the disposition of substantially all of the assets used by a corporation in a trade or business of such corporation, within the meaning of section 401(k)(10)(A)(ii).

2. The lump sum distribution by Plan X to former employees of Division G may be made pursuant to section 401(k)(2)(B)(ii)(II) of the Code without adversely affecting the tax treatment of salary deferrals under Plan X under section 402(e)(3),

Section 401(k)(2)(B)(i) of the Code provides that, in relevant part, that distributions from a qualified cash or deferred arrangement may not be made earlier than the occurrence of certain stated events. Section 401(k)(2)(B)(i)(II), when read together with 401(k)(10)(A)(ii) further provides that one of these distributable events is the disposition by a corporation of substantially all of the assets (within the meaning of section 409(d)(2)) used by such corporation in a trade or business of such corporation, but only with respect to an employee who continues employment with the corporation acquiring such assets.

Section 1.401(k)-1(d)(4) of the Income Tax Regulations provides rules applicable to distributions upon the sale of assets. This section provides, in part, that (i) the seller must maintain the plan, and the purchaser may not maintain the plan after the disposition; (ii) the employee must continue employment with the purchaser of the assets; (iii) distribution must be in connection with the disposition of the assets; (iv) the sale of substantially all the assets used in a trade or business means the sale of at least 85 percent of the assets. Section 1.401(k)-1(d)(5) provides, in part, that a distribution may be made only if it is a lump sum distribution within the meaning of section 402(d)(4) of the Code.

Section 402(e)(3) of the Code provides that an employee election to defer compensation in a 401(k) plan will be considered as an employer contribution.

In this case, Company B disposed of Division G, which, based upon the facts and circumstances presented herein, has been determined to be a trade or business as that term is used in section 401(k)(A)(ii) of the Code. Over 85 percent of the assets of Division G were sold to Company E. Company A will maintain Plan X after the sale. In addition, no assets or liabilities of Plan X have been transferred to a plan maintained by Company E. The proposed distributions from Plan X will be made as lump sum distributions to Plan X participants who are now employed by Company E.

Accordingly, with respect to ruling requests one and two, we conclude that (1) the disposition of Division G is the disposition of substantially all of the assets used by Company A in a trade or business within the meaning of section 401(k)(10)(A)(ii) of the Code; and (2) the lump sum distributions made by Plan X in connection with the above described disposition of assets may be made pursuant to section 401(k)(2)(B)(ii)(II) without adversely affecting the tax treatment of salary deferrals under Plan X under section 402(e)(3),

These rulings are based on the assumption that Plan X at all relevant times continues to be qualified under section 401(a) of the Internal Revenue Code.

A copy of this letter has been sent to your authorized representative, in a accordance with a power of attorney on file in this office.

Sincerely yours,

Frances V. Sloan

Frances V. Sloan
Chief, Employee Plans
Technical Branch 3

Enclosures:
Deleted Copy of Letter
Notice of Intention to Disclose